

Issue 61: INSIDER'S EDGE: How to Handle Self-Employment Income

Happy Friday, Insiders! Welcome to another issue of the Insider's Edge. Today, we'll be taking a look at how to handle reporting self-employment income.

As you know, when a consumer applies for benefits, they must provide income information for each member of their household who is required to file federal income taxes. So how should consumers who are self-employed provide information on their self-employment income?

What is Changing?

For Medicaid applications in the past, self-employment income was calculated by taking total self-employment income and dividing it in half to account for business expenses associated with the self-employment. Now, under MAGI (modified adjusted gross income) rules, consumers must use the IRS definition of what counts as self-employment income as well as what the IRS defines as appropriate deductions.



What Is Self-Employment Income?

Self-employment income is defined as the **net income** a person earns from their own trade or business. Self-employment income could also come from a distributive share from a partnership. Net income is the excess money a consumer makes after the business's operating expenses are deducted from the total amount of money the business received. **Net loss** is the excess of the business's allowable deductions that can be taken from the total amount of money the business received. (If the consumer is a partner, include his/her distributive share from the partnership.)

EXAMPLE: Any net income (profit) a consumer earns from goods they sell or services they provide to others counts as self-employment income. *Note that it is possible for self-employment income to be negative.* This occurs when expenses are more than the amount the person earns through self-employment activities.



Determining Net Income from Self-Employment

Determining net income from self-employment is a three step process.

1. First, the consumer will need to provide their total self-employment income.
2. Next, the consumer should provide the expenses that can be deducted from their self-employment income (see below).
3. Finally, to determine net self-employment income, subtract the total expenses that can be deducted from the total self-employment income.

(Total self-employment income)

– (Total expenses that can be deducted)

(Net self-employment income)

Information on an applicant's prior year self-employment income can be found on last year's federal income tax return Form 1040 on line 12 and on Schedule C or Schedule C-EZ. Some consumers may find this a useful reference point as they seek to provide their current self-employment income.



What Expenses Can Be Deducted from Self-Employment Income?

Consumers can deduct certain expenses from their self-employment income. Information on the consumer's deductions in the prior year can be found on last year's federal income tax return on IRS Form 1040 lines 27-29 and on and Schedule C or Schedule C-EZ.

Consumers may be able to deduct the following expenses paid to operate their business:

- Advertising
- Car and truck expenses (for travel during the work day, not commuting)
- Certain business travel and meals
- Commissions, taxes, licenses, and fees
- Contract labor
- Contributions to a self-employed SEP, SIMPLE, or qualified retirement plan
- Depreciation
- Deductible self-employment taxes
- Employee wages and fringe benefits
- Interest on loans for your business (including mortgage interest paid to banks)
- Legal and professional services
- Rent or lease of business property and utilities
- Repairs and maintenance
- Property, liability, or business interruption insurance

Additional Resources

To learn more about the different types of allowable deductions available to self-employed consumers, visit IRS.gov to view "Instructions for Schedule C" or read IRS Publication 334 (2012), pages 30-39, available at <http://www.irs.gov/pub/irs-pdf/p334.pdf>.

Questions? Send them my way to dhmh.medicaidmarge@maryland.gov.